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Supreme Court of the United States

OCTOBER TERM, 1942.

No. 190

EDMUND WRIGHT GINSBERG CORPORATION,
Petitioner,

vs.

JOHN M. SWETNAM, as Trustee in Bankruptcy of The Deford Company.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

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INDEX.

Subject Index.

	PAGE
Petition for Writ of Certiorari	1
Opinions below	2
Jurisdiction	2
Questions presented	2–3
Statutes involved	3–4
Statement	4–10
Specification of errors to be urged	11
Reasons for granting the writ	12–37
I. The Circuit Court of Appeals exceeded its power when it ignored Rule 52(a) of the Federal Rules of Civil Procedure, reviewed the evidence *de novo* and set aside findings of fact not clearly erroneous	12–18
II. The Supreme Court should resolve the confusion among the Circuits as to the effect of findings of fact under Rule 52(a)	18–21
III. Findings of fact, establishing there was no reasonable cause to believe a preference was effected, were supported by substantial evidence, the weight of the evidence, and were not clearly erroneous	21–25
IV. Findings of fact, establishing a valid pledge were supported by substantial evidence, the weight of the evidence, and were not clearly erroneous	25–32
V. The Circuit Court of Appeals, in deciding that a pledge may not be perfected by taking possession of the proceeds of the pledged property, held contrary to the applicable decisions of this Court and in conflict with decisions of other Circuit Courts of Appeal	32–37

TABLE OF CITATIONS.

Cases.

	PAGE
Andrew Jergens Co. v. *Connor,* 125 F. (2d) 686 (C. C. A. 6th, 1942)	18
Barber Asphalt Paving Company v. *Standard Asphalt & Rubber Company,* 274 U. S. 728 (1927), cert. granted; 275 U. S. 372 (1927)	13
Border Nat. Bank v. *Coupland,* 240 Fed. 355 (C. C. A. 5th, 1917)	36
Britton v. *Union Inv. Co.,* 262 Fed. 111 (C. C. A. 8th, 1919), cert. den. 252 U. S. 580 (1920)	35
Chicago & N. W. R. Co., In re, 110 F. (2d) 425 (C. C. A. 7th, 1940)	20
Coppard v. *Martin,* 15 F. (2d) 743 (C. C. A. 5th, 1926), cert. den. 273 U. S. 753 (1927)	36
Crosby v. *Packer,* 22 F. (2d) 611 (C. C. A. 1st, 1927)	36
Fairbanks, Morse & Company v. *American Valve & Meter Company,* 274 U. S. 735 (1927), cert. granted; 276 U. S. 305 (1928)	13
Finance and Guaranty Company v. *Oppenhimer,* 276 U. S. 10 (1928)	33
Fleming v. *Palmer,* 123 F. (2d) 749 (C. C. A. 1st, 1941)	19
Glover Specialties Co., In re, 18 F. (2d) 314 (D. Conn., 1927)	22
Goldstein v. *Rusch,* 56 F. (2d) 10 (C. C. A. 2d, 1932), cert. den. 287 U. S. 604 (1932)	22
Halliday v. *United States,* 86 L. Ed. 393 (1942)	13
Irving Trust Co. v. *Bank of America Nat. Ass'n.,* 68 F. (2d) 887 (C. C. A. 2d, 1934)	36
Kennard v. *Behrer,* 270 Fed. 661 (S. D. N. Y., 1920)	22
Knapp v. *United States,* 110 F. (2d) 420 (C. C. A. 7th, 1940)	15

PAGE

Krauss Brothers Lumber Company v. *Mellon*, 275 U. S. 513 (1927), cert. granted; 276 U. S. 386 (1928) 13

Kuhn v. *Princess Lida of Thurn & Taxis*, 119 F. (2d) 704 (C. C. A. 3rd, 1941) 20, 21

Manning v. *Gagne*, 108 F. (2d) 718 (C. C. A. 1st, 1939) 19

MacDonald v. *Aetna Indemnity Co.*, 90 Conn. 415, 97 A. 332 (1916) 22

McDougal v. *Central Union Conference Assoc.*, 110 F. (2d) 939 (C. C. A. 10th, 1940) 22

Missouri Pac. Transp. Co. v. *George*, 114 F. (2d) 757 (C. C. A. 8th, 1940), cert. den. 312 U. S. 681 (1941) 19

Nathan and Cohen, In re, 58 F. (2d) 670 (S. D. N. Y., 1932), rev. 68 F. (2d) 864 (C. C. A. 2d, 1934) 28

National Labor Rel. Board v. *Waterman S. S. Corp.*, 309 U. S. 206 (1940) 13

Occidental Life Ins. Company v. *Thomas*, 107 F. (2d) 876 (C. C. A. 9th, 1939) 20

Page v. *Rogers*, 211 U. S. 575 (1909) 34

Plack v. *Baumer*, 121 F. (2d) 676 (C. C. A. 3rd, 1941) 19

Pyle v. *Texas Transport & Terminal Co.*, 238 U. S. 90 (1915) 21, 25

Ryttenberg v. *Scheffer*, 131 Fed. 313 (S. D. N. Y., 1904) 22

Sawyer v. *Turpin*, 91 U. S. 114 (1875) 34

Sexton v. *Kessler*, 172 Fed. 535 (C. C. A. 2d, 1909) 22

Storley v. *Armour & Co.*, 107 F. (2d) 499 (C. C. A. 8th, 1939) 14

Swetnam v. *Edmund Wright Ginsberg Corp.*, 37 F. Supp. 546 (S. D. N. Y., 1941) rev. (not yet reported) 2, 4

Thompson v. *Fairbanks*, 196 U. S. 516 (1905) 33

Union Trust Company of Maryland v. *Townshend*, 101 F. (2d) 903 (C. C. A. 4th, 1939), cert. den. 307 U. S. 646 22

PAGE

U. S. v. *Mitchell*, 104 F. (2d) 343 (C. C. A. 8th, 1939) 20

Webb v. *Frisch*, 111 F. (2d) 887 (C. C. A. 7th, 1940) 15, 20, 32

Wilmington Trust Co. v. *Helvering*, 86 L. Ed. 908 (1942) 12

Wright-Dana Hardware Co., In re, 212 Fed. 397 (C. C. A. 2d, 1914) 22

STATUTES.

48 Stat. 1064, 28 U. S. C. A., sec. 723(b),(c) 3

Bankruptcy Act, sec. 60(b), prior to *Chandler Act* 4, 21

Judicial Code, sec. 240(a), 28 U. S. C. A., sec. 347(a) 2

Virginia Code of 1936, sec. 5224 (Virginia Traders Act) 10, 31

FEDERAL RULES.

Federal Rules of Civil Procedure, Rule 52 (a) 2, 3, 10, 11, 12, 14, 15, 17, 18, 22, 32

MISCELLANEOUS.

Advisory Committee on Rules of Civil Procedure Report of May, 1937 21

28 Columbia Law Review 943 (1928), Note 36

Federal Rules of Civil Procedure and Proceedings of the American Bar Association Institute, Cleveland, July, 1938 15, 16

Federal Rules of Civil Procedure. Proceedings of Institutes. Washington and New York, (1938) 17, 18

Preliminary Draft of Rules of Civil Procedure for the District Court, etc., prepared by the Advisory Committee, May 1936 15

4 Remington on Bankruptcy, 4th Ed., sec. 1828 22

Review of Facts under Proposed Federal Rules, 20 Journal of American Judicature Society 129 17

Review of Findings of Fact, 4 University of Chicago Law Review 17

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No. .....

EDMUND WRIGHT GINSBERG CORPORATION,

Petitioner,

v.

JOHN M. SWETNAM, as Trustee in Bankruptcy of The Deford Company.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

Edmund Wright Ginsberg Corporation prays that a Writ of Certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered in the case entitled, "John M. Swetnam, as Trustee in Bankruptcy of The Deford Company, Appellant, *v.* Edmund Wright Ginsberg Corporation, Appellee" on May 26, 1942, reversing the decision of the United States District Court for the Southern District of New York.

Opinions Below.

The opinion of the United States District Court for the Southern District of New York (R. 315) is reported in 37 Fed. Supp. 546. The opinion of the Circuit Court of Appeals (R. 346) is not yet reported.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered May 26, 1942 (R. 378). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925; 28 U. S. C. A. Section 347(a).

Questions Presented.

(1) Whether under Rule 52(a) of the Federal Rules of Civil Procedure, which provides that in a case, as here, tried without a jury, the Trial Court shall "find the facts specially", and such facts shall not be set aside "unless clearly erroneous", the Circuit Court of Appeals exceeded its power in reviewing the evidence *de novo* and

(a) deciding there was a voidable preference under Section 60(b) of the Bankruptcy Act (prior to the amendment known as the Chandler Act), when the Trial Court had "specially" made findings of fact establishing no reasonable cause to believe the transfers would effect a preference, and such findings of fact were supported by substantial evidence and the weight of the evidence and were not "clearly erroneous";

(b) deciding there was no valid pledge of the property in question when the Trial Court had "specially" made findings of fact establishing that there

was a valid pledge, and such findings of fact were supported by substantial evidence and the weight of the evidence and were not "clearly erroneous".

(2) Whether the Circuit Court of Appeals has decided the issue of perfecting a pledge by taking possession of the proceeds of the property pledged, contrary to (a) decisions of this Court and (b) in conflict with decisions of other Circuit Courts of Appeal.

Statutes Involved.

(1) The Act of June 19, 1934, Ch. 651, §§1 and 2, 48 Stat. 1064 (28 U. S. C. A. Sec. 723(b), (c)), under which the Supreme Court of the United States has power to prescribe "by general rules, for the district courts of the United States, * * * the practice and procedure in civil actions at law," and "to unite the general rules prescribed by it for cases in equity with those in actions at law, so as to secure one form of civil action and procedure for both".

(2) Rule 52(a) of the Federal Rules of Civil Procedure (promulgated pursuant to the authority of the above quoted statutes), reading as follows:

> "In all actions tried upon the facts without a jury, the court shall find the facts specially and state separately its conclusions of law thereon and direct the entry of the appropriate judgment; and in granting or refusing interlocutory injunctions the court shall similarly set forth the findings of fact and conclusions of law which constitute the grounds of its action. Requests for findings are not necessary for purposes of review. Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses. The findings of a master, to the extent that the court adopts them,

shall be considered as the findings of the court" (28 U. S. C. A. following §723c).

(3) Section 60(b) of the Bankruptcy Act (before the Chandler Act), reading as follows:

> "If a bankrupt shall have procured or suffered a judgment to be entered against him in favor of any person or have made a transfer of any of his property, and if, at the time of the transfer, or of the entry of the judgment, or of the recording or registering of the transfer if by law recording or registering thereof is required, and being within four months before the filing of the petition in bankruptcy or after the filing thereof and before the adjudication, the bankrupt be insolvent and the judgment or transfer then operate as a preference, and the person receiving it or to be benefited thereby, or his agent acting therein, shall then have reasonable cause to believe that the enforcement of such judgment or transfer would effect a preference, it shall be voidable by the trustee and he may recover the property or its value from such person. * * * (July 1, 1898, c. 541, §60, 30 Stat. 562; Feb. 5, 1903, c. 487, §13, 32 Stat. 799; June 25, 1910, c. 412, §11, 36 Stat. 842)" 11 U. S. C. A. §96(b).

Statement.

This is an action by John M. Swetnam, as Trustee in Bankruptcy of The Deford Company, herein called "Deford", against Edmund Wright Ginsberg Corporation, for the recovery of an alleged preference, under Section 60(b) of the Bankruptcy Act before its amendment by the Chandler Act. The case was tried before the Honorable Mortimer W. Byers, United States District Judge, without a jury, who after hearing all the evidence, found facts specially, pursuant to Rule 52(a) F. R. C. P., establishing

among other things that Petitioner had a valid common law pledge lien, and that Petitioner did not have reasonable cause to believe that by the assignment of the proceeds of the pledged property (the accounts) a preference was being effected.

The findings of fact by the Trial Court (R. 329 to 336, inclusive) give a summary of the case. Accordingly, we set them out at length, as follows:

> I. That the plaintiff is the trustee in bankruptcy of the Deford Company (hereinafter called "Deford"), a West Virginia Corporation which was adjudicated a bankrupt on the 20th day of July, 1938, in the Western District of Virginia.
>
> II. Deford was at all times here in question engaged in the business of buying hides, tanning the hides into leather and selling the leather, and its business office was at Baltimore, Md., and its tannery at Luray, Va.
>
> III. That the defendant is a New York corporation which at all times here in question was engaged in the business of commercial factoring.
>
> IV. That Deford, in order to obtain working capital, entered into a contract with defendant dated November 25, 1936, to be effective as of October 14, 1936 (hereinafter called "the contract") by which defendant agreed to make advances to Deford, to be secured by a lien on all of Deford's hide and leather inventory, and which leather was to be sold by Deford, and the accounts receivable arising therefrom to be assigned to defendant and to become the property of defendant as they were created.
>
> V. That the contract further provided that in order that defendant should have exclusive possession and dominion of the pledged property, Deford was to lease to defendant certain buildings described and

numbered on a map of the Manufacturers Appraisal Company as No. 14 (frame hide house), No. 17 (leather warehouse), No. 22 (leather warehouse), No. 55 (leather warehouse) and No. 25 (warehouse office).

VI. That as provided in the contract, and subject to its terms, agreements and covenants, a lease dated December 29, 1936 of said buildings, Nos. 14, 17, 22, 55 and 25, was made by Deford to defendant commencing as of October 14, 1936 and ending December 31, 1938.

VII. That as required in the contract, notice of the factoring arrangment was given to the Federal Reserve Bank of Richmond, Richmond, Virginia, and said bank assented to the contract and the lease made pursuant thereto.

VIII. That notice that Deford was pledging with defendant hides and leather as collateral security for loans, and that all accounts receivable arising from shipments of leather by Deford were assigned to defendant, was published twice a week for two weeks, in December, 1936, in the Page News and Courier of Luray, Virginia.

IX. That all requisite publicity and notoriety was given by Deford and defendant regarding their contractual transactions.

X. That pursuant to the terms of the contract, and at all times here involved, signs of about 16 inches by 4 inches were erected and maintained conspicuously inside and were displayed outside the buildings leased to defendant by Deford, and on the door of Deford's main tannery office, the signs on the outside reading "Edmund Wright Ginsberg Corporation, Factor for the Deford Company", and the signs on the inside reading "All Leather in This Warehouse is Pledged to Edmund Wright Ginsberg Corporation."

XI. That insurance carried by Deford on its hide and leather inventory was made payable to defendant as its interest might appear.

XII. That, in accordance with the provisions of the contract one John B. Long was appointed by defendant its custodian of the hides and leather pledged by Deford with defendant.

XIII. That Long entered the employ of defendant on November 1, 1936, at which time his previous employment by the Deford Company was terminated, and from November 1, 1936 acted in behalf of defendant as its custodian of the hides and leather pledged with defendant and he asserted on its behalf custody and possession of such pledged property.

XIV. That Long's salary was charged back by defendant to Deford at the end of the year 1937, but that there was no charge back for his salary during 1938, in which year the cost of his employment was borne entirely by defendant.

XV. That pursuant to the terms of the contract, and at all times here involved, all hides delivered to Deford were stamped with defendant's symbol, and such hides and leather tanned therefrom were consigned and delivered to defendant by Deford.

XVI. That at all times here involved there was no hide or leather inventory in the Deford plant except such as was purchased and processed with money furnished by defendant and consigned and delivered to the defendant.

XVII. That as finished leather resulted from the tanning operations at the Deford plant, it was delivered into the warehouses leased to defendant, buildings Nos. 17, 22 and 55, and there stored in such possession, custody and control of defendant until sold by Deford.

XVIII. That pursuant to the terms of the contract, Deford sold the pledged leather and shipments thereof were made from the warehouses leased to defendant,

only pursuant to instructions of the Baltimore office of Deford, except for a few sales for cash by Kendrick.

XIX. That the Baltimore office of Deford gave no instructions for the shipment of leather from warehouses leased to defendant without first having or securing the approval of defendant to sale of such leather prior to sale and shipment thereof.

XX. That defendant supervised and advised concerning the sale of leather consigned to it by Deford through its credit department.

XXI. That during the period of four months immediately preceding the petition in bankruptcy of Deford, there were no tanning operations at the Deford plant, but said plant was inactive and all leather on hand was stored in the warehouses leased to defendant and was then in defendant's possession, custody and control.

XXII. That all accounts receivable arising out of the sale of leather by Deford were immediately assigned to and became the property of defendant as they arose, and that invoices relating thereto showed on the face thereof that they were assigned and payable directly to defendant.

XXIII. During said period of four months immediately preceding the petition in bankruptcy of Deford the accounts assigned to defendant arose from sales of the leather consigned to defendant and stored in the warehouses leased to the defendant, which leather was in defendant's possession, custody and control as collateral security for advances made to Deford, and said accounts were substituted for said collateral in liquidation of said advances.

XXIV. That Deford and defendant at all times believed, and reasonably believed and understood, and acted upon said belief and understanding that all hides

and leather in the Deford plant were subject to a lien of defendant as collateral security for advances made by defendant to Deford, and that accounts receivable arising therefrom were the property of defendant, all as agreed on in the contract between Deford and defendant, and that the accounts assigned to defendant in the four months preceding the bankruptcy of Deford were assigned to defendant in the regular course of the business dealings between Deford and defendant and as provided in said contract.

XXV. That the aggregate amount of advances made by Deford to defendant (*sic*) over the entire period of the transactions between them under the contract, exceeded $1,000,000.

XXVI. That in April, 1938, Deford and defendant had communications and discussions concerning further advances to Deford by defendant and the reopening of the Deford plant.

XXVII. That in 1937, prominent mercantile agencies, namely Dun & Bradstreet, the Feakes Mercantile Agency, Inc., and the Shoe & Leather Mercantile Agency, Inc. were informed of and issued reports concerning the fact that defendant was acting as factor for Deford, making advances against inventory, and taking assignments of accounts receivable.

XXVIII. That most of the claims filed in the Deford bankruptcy were those of bond and debenture holders, and only a small percentage were those of merchandise creditors.

XXIX. That Deford's tannery was located in a rural community and consisted of many buildings scattered over the property, and that such tannery was remote from the paths of trade, and the opportunity of creditors being misled to their detriment by any conditions at the Deford plant was lacking.

XXX. That there was in force and effect at all times here involved a Virginia statute known as the

Traders Act, being Section 5224 of the Virginia Code of 1936, and reading as follows:

> "If any person transact business as a Trader, with the addition of the words 'factor', 'agent', 'and company', or 'and Co.', and fail to disclose the name of the principal or partner by a sign in letters easy to read, placed conspicuously at the house wherein such business is transacted, and also by a notice published for two weeks in a newspaper (if any) printed in the city, town or county wherein the same is transacted; or if any person transact such business in his own name, without any such addition; all the property, stock, and choses in action acquired or used in such business shall, as to the creditors of any such person, be liable for the debts of such person. This section does not apply to a person transacting such business under a license to him as an auctioneer or commission merchant."

XXXI. That the contract was not unfair to Deford's creditors and was adhered to in all matters of performance with reasonable fidelity and both Deford and defendant acted thereunder openly and in good faith.

The Circuit Court of Appeals, without even mentioning Rule 52(a), reversed the judgment of the Trial Court, and thus set aside decisive findings of fact (R. 346). The findings were not even referred to in the opinion of the Circuit Court of Appeals and were not stated or found to be "clearly erroneous", or unsupported by substantial evidence or the weight of the evidence. A petition for rehearing was filed but was denied (R. 377).

Specification of Errors to Be Urged.

The Circuit Court of Appeals erred:

1. In ignoring Rule 52(a) of the Federal Rules of Civil Procedure, reviewing the evidence *de novo* and setting aside the Trial Court's findings of fact which were not clearly erroneous.

2. In deciding there was a voidable preference where the findings of fact, supported by substantial evidence and the weight of the evidence and not clearly erroneous, established there was no reasonable cause to believe a preference would be effected under Section 60(b) of the Bankruptcy Act as it existed prior to the Chandler Act.

3. In deciding there was not a valid pledge where the findings of fact, supported by substantial evidence and the weight of the evidence and not clearly erroneous, established that there was a valid pledge.

4. In deciding the pledge, if imperfect, was not perfected, by the taking of possession of the proceeds of the property pledged, contrary to (a) decisions of this Court and (b) in conflict with decisions of other Circuit Courts of Appeal.

REASONS FOR GRANTING THE WRIT.

I.

The Circuit Court of Appeals exceeded its power when it ignored Rule 52(a) of the Federal Rules of Civil Procedure, reviewed the evidence *de novo* and set aside findings of fact not clearly erroneous.

The United States Supreme Court has never decided what effect the Circuit Court of Appeals must give to findings of fact under Rule 52(a) of the Federal Rules of Civil Procedure, which provides, in part, as follows:

> "Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses."

This is an "important question of law" and "should be settled by this Court" since it deals with the power of the Circuit Courts of Appeal.

The United States Supreme Court granted certiorari in the recent case of *Wilmington Trust Co.* v. *Helvering,* 86 L. Ed. 908 (1942), so as to bring up the question of the interpretation of a federal statute defining the effect of findings of fact of the Board of Tax Appeals when reviewed by a Circuit Court of Appeals. In that case, the Third Circuit had set aside findings of fact made by the Board of Tax Appeals, the findings dealing with what constituted a "short sale", and the Supreme Court reversed the Third Circuit, saying at page 911:

> "It is the function of the Board, not the Circuit Court of Appeals, to weigh the evidence, to draw inferences from the facts, and to choose between conflicting inferences. The court may not substitute its view of the facts for that of the Board. Where

> the findings of the Board are supported by substantial evidence they are conclusive. Helvering *v.* F. & R. Lazarus & Co., *supra;* Helvering *v.* Kehoe, 309 U. S. 277, 84 L. ed. 751, 60 S. Ct. 549, and cases cited."

The Supreme Court granted certiorari in the case of *National Labor Rel. Board* v. *Waterman S. S. Corp.*, 309 U. S. 206 (1940), so as to bring up the analogous issue of the effect to be given to findings of fact of the National Labor Relations Board under a federal statute.

In the instant case, the question is whether the Circuit Court of Appeals has not usurped the function of the trial court in violation of Rule 52(a) of the Federal Rules of Civil Procedure. It is of paramount importance, if we are to have an orderly, efficient, judicial administration, that the appellate courts not encroach upon the power of the trial courts.

Certiorari has also been granted in many cases where the meaning of an important rule of federal practice was involved.

See: *Halliday* v. *United States,* 86 L. Ed. 393 (1942), certiorari granted (meaning of Rule 50(b) of the Federal Rules of Civil Procedure was involved); *Barber Asphalt Paving Company* v. *Standard Asphalt & Rubber Company,* 274 U. S. 728 (1927), cert. granted; 275 U. S. 372 (1927) (meaning of Federal Equity Rule 75(b) reviewed); *Fairbanks, Morse & Company* v. *American Valve and Meter Company,* 274 U. S. 735 (1927), cert. granted; 276 U. S. 305 (1928) (meaning of Federal Equity Rule 75(b) reviewed); *Krauss Brothers Lumber Company* v. *Mellon,* 275 U. S. 513 (1927), cert. granted "limited to the question of practice in respect to the bill of exceptions upon which the case in the Circuit Court of Appeals was made to turn"; 276 U. S. 386 (1928) (federal practice in respect to a bill of exceptions reviewed.)

That the power of the Circuit Court of Appeals to review is restricted by Rule 52(a) cannot be questioned. The Rule makes findings of fact of the trial court final, unless they are "clearly erroneous". Under this Rule, the evidence certainly cannot be reviewed *de novo* by a Circuit Court of Appeals. Only the *findings of fact* can be reviewed, and such review is limited by the effect Rule 52(a) gives such findings.

Although the above is clear from a reading of Rule 52(a), nevertheless, the Circuit Court of Appeals in the instant case reviewed the evidence *de novo,* set aside decisive findings of fact of the Trial Court and reached a conclusion predicated upon inconsistent findings of its own. Strangely, the Circuit Court of Appeals nowhere in its opinion referred to Rule 52(a). No mention is made in the entire opinion of the findings of fact of the Trial Court, nor does the opinion, at any place, state that any finding of fact of the Trial Court was "clearly erroneous" or unsupported by substantial evidence. It will later be shown (pp. 21 to 33) that the findings of fact establishing there was no reasonable cause to believe a preference was effected, and that there was a valid pledge, were actually supported by substantial evidence, the weight of the evidence, and were not clearly erroneous.

The Circuit Court of Appeals misconceived its power in the instant case. Its jurisdiction is appellate, and, as was held in *Storley* v. *Armour & Co.,* 107 F. (2d) 499, 513 (C. C. A. 8th, 1939):

> "It is not the function of this Court to retry this case and to pass upon questions of fact the determination of which depended upon the credibility of witnesses and the weight of evidence, or to substitute its judgment for that of the trier of the facts which had reached permissible conclusions. See

> Helvering *v.* Johnson, 8 Cir., 104 F. 2d 140, 144, and cases cited, and Rule 52(a) of the Rules of Civil Procedure for the District Courts of the United States, 28 U. S. C. A. following section 723c."

It should not have passed on the evidence *de novo;* it only has the power to review the findings of fact, and, regardless of whether it agrees with them, it can set them aside only if they are "clearly erroneous". The correct principle was stated in *Webb* v. *Frisch,* 111 F. (2d) 887 (C. C. A. 7th, 1940), as follows:

> "We do not understand that the foregoing rule (Rule 52) has enlarged the discretion of this Court in passing upon the probative force of evidence. Our function is to review the finding of the lower court and not to pass upon the evidence *de novo.* We cannot say that a finding of the fact of prior use is 'clearly erroneous' merely because we might have entertained some doubt about the quantum of evidence."

See also: *Knapp* v. *United States,* 110 F. (2d) 420 (C. C. A. 7th, 1940).

Rule 52(a) first appeared as proposed Rule 68, in the Preliminary Draft of Rules of Civil Procedure for the District Courts, etc., prepared by the Advisory Committee, May 1936. Proposed Rule 68 read: "The findings of the court in such cases shall have the same effect as that heretofore given to findings in suits in equity" but later became present Rule 52(a), which now reads: "the findings of fact shall not be set aside unless clearly erroneous".

Mr. William D. Mitchell, who had been designated by the Supreme Court as Chairman of the Advisory Committee on Rules of Civil Procedure, said before the American Bar Association Institute, held at Cleveland on July 22, 1938, at page 318:

> "In the present modern Equity Rule—I think I can state almost the exact language that the Supreme Court has used in many cases—the findings of the trial judge are presumptively correct and shall not be set aside unless clearly erroneous, and in all cases where witnesses are called orally and their credibility is involved, due regard shall be given to the opportunity of the trial court to pass on their credibility. That is the modern Equity Rule.
>
> "We struck out the phrase 'presumptively correct' because these law school fellows told us it didn't mean anything anyway. We left in the phrase 'unless clearly erroneous'. That applies under these rules to every case tried by a judge without a jury, whether it is a law case or an equity case.
>
> * * * * * *
>
> "We adopted the modern equity rule, and this rule applies whether there is a conflict of evidence or whether there is a difference of opinion as to inference that may be drawn from undisputed evidence."

And further, at page 383, he said:

> "But of course Rule 52(a) specifies the test that will be applied in appellate courts in passing on the question of whether findings are sustained by the evidence, and the test is whether they are clearly erroneous or not; in other words, the test is whether the weight of the evidence is clearly against the findings."
>
> (Federal Rules of Civil Procedure and Proceedings of the American Bar Association Institute, Cleveland, pp. 318, 383.)

Members of the Advisory Committee differed as to the effect to be given on appeal to findings of fact. Judge Charles E. Clark, who wrote the opinion in the instant case, advocated adoption in all appeals of the rule giving findings of fact by a judge without a jury the same binding effect as

findings of fact by a verdict of a jury. He contended that if the equity rule were adopted, it would reduce trial judges to mere automatons, and would give appellate courts very extensive powers. In an article entitled "Review of Facts under Proposed Federal Rules" (20 J. Am. Jud. Soc. 129 at 130), Judge Clark says:

> "Carried to its logical conclusion, the full review would make of the judge only a notary to supervise the transcribing of evidence. There would seem to be no reason why for like reasons to those applying in case of the administrative officer, he should not be given the power to end the case unless manifest error is apparent. That is the job for which he is designated; if he is worthy of his position at all he should be more than a mere automaton."

And, Judge Clark, in 4 University of Chicago Law Review 190, in an article entitled "Review of Findings of Fact", at pages 214 and 217, says:

> "The equity review treats the trial judge with no more favor than were administrative experts under some, at least, of the earlier acts, now definitely being superseded.
>
> • • • • • • •
>
> "It does afford a fairly flexible system not bound by definite rule, with potentially at least very extensive power in the appellate court."

Thus it will be seen that Judge Clark then was of the opinion that under Rule 52(a) the Circuit Courts of Appeal would have power to review the evidence *de novo* whereas Mr. Mitchell, at the New York Symposium on Federal Rules, October 18, 1938 said at page 287:

> "The Committee chose the broader view so that this rule now applying to all cases tried by a judge without a jury is practically the modern equity rule; it is not the ancient equity rule which allowed a trial *de*

novo on the facts in the appellate court—it is a limited provision—the appellate court may not set aside the findings unless they are clearly erroneous or against the clear weight of evidence." Federal Rules of Civil Procedure. Proceedings of Institutes. Washington and New York, 1938.

The Circuit Court of Appeals in the instant case, instead of considering whether there was a valid pledge or voidable preference based upon its *review of the findings of fact* giving them the effect prescribed in Rule 52(a), erroneously considered whether there was a valid pledge or voidable preference based on its *review of the evidence de novo,* without giving any effect to the findings of fact or Rule 52(a). Looking at the question in this manner, the Circuit Court of Appeals treated the Trial Court as a mere automaton through whom the case had passed, but to whose findings of fact and decision no effect need be given. Certainly Rule 52(a) does not treat findings of fact in this manner and give the Circuit Courts of Appeal such power. If findings of fact of the Trial Court are not to be treated under Rule 52(a) as in the instant case then it is important for the Supreme Court to make such a pronouncement, so that the District Courts, the Circuit Courts of Appeal and litigants can guide themselves accordingly.

II.

The Supreme Court should resolve the confusion among the Circuits as to the effect of findings of fact under Rule 52(a).

The meaning of the expression "Findings of fact shall not be set aside unless clearly erroneous" in Rule 52(a) is a source of confusion among the various Circuits and should be clarified by this Court. In *Andrew Jergens Company* v. *Connor,* 125 F. (2d) 686 (1942), the Sixth Circuit

Court of Appeals states the meaning of the rule at page 689 as follows:

> "Where a case is tried by the court, a jury having been waived, the court's findings upon questions of fact are conclusive upon appeal, no matter how convincing the argument that upon the evidence the findings should have been different unless there is no substantial evidence to support them. We are bound by the lower court's findings unless they are clearly erroneous. Federal Rules of Civil Procedure rule 52. * * *"

In *Plack* v. *Baumer*, 121 F. (2d) 676 (1941), the Third Circuit Court of Appeals states the rule similarly:

> "These findings, which, as we have said, are supported by substantial evidence, may not now be disturbed. Rule 52(a) Federal Rules of Civil Procedure. * * *"

But, the First Circuit Court of Appeals, in *Manning* v. *Gagne*, 108 F. (2d) 718 (1939), rejects the substantial evidence rule and says:

> "The trial was without jury, and in such cases, the 'substantial evidence' rule no longer applies. By virtue of the Federal Rules of Civil Procedure * * * the applicable test is whether * * * the finding was 'clearly erroneous'. Rule 52(a)."

and the same Court said in *Fleming* v. *Palmer*, 123 F. (2d) 749, 751 (1941):

> "A finding of fact is clearly erroneous if it is against the clear weight of evidence. It does not suffice that it is supported by evidence."

The Eighth Circuit Court of Appeals in *Missouri Pac. Transp. Co.* v. *George*, 114 F. (2d) 757 (1940), cert. den. 312 U. S. 681, would not accept the preponderance or weight of the evidence rule, and said:

> "The findings are based upon conflicting testimony. The appellants' contention is that the quoted finding is not supported by a preponderance of the evidence. We have examined the evidence, and the quoted finding is supported by substantial evidence. It is not, therefore, clearly erroneous. It can not for that reason be set aside by this court. Rule 52(a), Rules of Civil Procedure."

A concurring opinion of the Ninth Circuit Court of Appeals, in *Occidental Life Insurance Company* v. *Thomas,* 107 F. (2d) 876 (1939), says:

> "Questions as to the weight of the evidence are not to be decided by us. The only question before us is whether or not the finding of the trial court is clearly erroneous. * * * I believe it is apparent that reasonable men would differ in making inferences from the evidence before us, and therefore the finding is not clearly erroneous."

And, finally we have the Second Circuit Court of Appeals in the instant case passing on the evidence *de novo* and ignoring the findings of fact in direct conflict with the Circuit Court of Appeals for the Seventh Circuit in *Webb* v. *Frisch,* 111 Fed. (2d) 887 (1940), which held:

> "Our function is to review the finding of the lower court, and not to pass upon the evidence *de novo.*"

Although the evidence in the instant case is disputed, confusion does exist as to the effect of findings of fact where the evidence is undisputed. Despite the clear wording of Rule 52 (a), some courts have stated that in this situation little weight is to be given to the findings of the Trial Judge. See *In re Chicago & N. W. R. Co.,* 110 F. (2d) 425 (C. C. A. 7th, 1940); *U. S.* v. *Mitchell,* 104 F. (2d) 343 (C. C. A. 8th, 1939); *Kuhn* v. *Princess Lida of Thurn*

& Taxis, 119 F. (2d) 704 (C. C. A. 3rd, 1941). The Advisory Committee, however, has stated that the Trial Court's findings of fact were to be equally binding in cases where testimony is undisputed as where it is conflicting. See *Advisory Committee's Report of May, 1937,* containing note to Supreme Court on Rule 52 (a). This was likewise stated to be the rule, in Chairman Mitchell's remarks before the American Bar Institute in Cleveland, quoted, *ante,* page 16.

Certiorari should be granted so that this confusion can be finally resolved.

III.

Findings of fact, establishing there was no reasonable cause to believe a preference was effected were supported by substantial evidence, the weight of the evidence, and were not clearly erroneous.

Section 60(b) of the Bankruptcy Act, prior to the Chandler Act (not effective when accounts in question were assigned), is the governing law in this case. Under it a preference is not voidable unless the Trustee of Deford has proved *as a fact* that the Petitioner upon receiving the accounts "shall then have reasonable cause to believe that the enforcement of such * * * transfer would effect a preference." *Pyle* v. *Texas Transport & Terminal Co.,* 238 U. S. 90 (1915). After the Chandler Act, the person receiving the property need only have "reasonable cause to believe that the debtor is insolvent." Findings of Facts XXIV, XXVI and XXXI (R. 334-335) established that the Petitioner had no reasonable cause to believe it was taking a preference when it received the accounts. Notwithstanding these findings of fact, not clearly erroneous, as we later show, the Circuit Court of Appeals nevertheless decided there was

a voidable preference under Section 60(b), saying only that "When the assignment was made, a preference was created. Under §60b, 11 U. S. C. A. §96b this was voidable."

Where a creditor receives the proceeds of a pledge, reasonably believing he has a valid pledge, he does not have reasonable cause to believe a preference is thereby being effected, notwithstanding the fact the pledge is invalid. *Ryttenberg* v. *Scheffer,* 131 Fed. 313, 317 (S. D. N. Y. 1904). Other cases have regularly applied the same principle. *Goldstein* v. *Rusch,* 56 F. (2d) 10 (C. C. A. 2d, 1932), cert. den. 287 U. S. 604; *In re Glover Specialties Co.,* 18 F. (2d) 314 (D. Conn., 1927); *MacDonald* v. *Aetna Indemnity Co.,* 90 Conn. 415, 97 A. 332 (1916); *Sexton* v. *Kessler,* 172 Fed. 535, 539 (C. C. A. 2d, 1909) affd. 225 U. S. 90; *Union Trust Company of Maryland* v. *Townshend,* 101 F. (2d) 903 (C. C. A. 4th, 1939), cert. den. 307 U. S. 646.

Actual knowledge by the creditor of the debtor's insolvency does not constitute reasonable cause to believe. *Kennard* v. *Behrer,* 270 Fed. 661 (S. D. N. Y., 1920); *In re Wright-Dana Hardware Co.,* 212 Fed. 397 (C. C. A. 2d, 1914). To the same effect, see 4 *Remington on Bankruptcy,* 4th Ed., Sec. 1828.

Applying Rule 52(a) to a preference case, the Court in *McDougal* v. *Central Union Conference Assoc.,* 110 F. (2d) 939, 942 (C. C. A. 10th, 1940), said:

> "The finding of the trial court that appellee did not have reason to believe that a preference would result from this conveyance is sustained by substantial testimony and cannot be disturbed on appeal."

The evidence shows that from the date of the initiation of the business between Petitioner and Deford, there was an agreement for a pledge of hides and leather, the sale thereof, and for the resulting accounts receivable to be the

property of the Petitioner; that the parties conducted business during the four months period in the same manner as prior thereto, adhered to the contract, and that the accounts receivable transferred to the Petitioner during the four months period were proceeds of leather pledged to Petitioner under the contract.

There is summarized below some of the voluminous evidence of the conduct of the parties, showing Petitioner had good reason to believe it had a valid pledge of the leather, and the accounts arising therefrom:

(a) The contract between the Petitioner and Deford provided these accounts receivable were to immediately become the property of Petitioner upon the sale of finished leather out of which they arose (Dfts. Ex. A., R. 218, 228).

(b) These accounts were assigned on schedules by Deford to Petitioner, and this was the regular course of conduct from the time the parties entered into the foregoing contract (R. 56-57; Dfts. Ex. J, R. 268).

(c) The invoices evidencing each of these accounts receivable showed thereon in clear and unmistakable language that they had been assigned and were payable *exclusively* to the Petitioner (R. 58; Dfts. Ex. K, R. 268).

(d) The credit of each of the debtors on these accounts had been approved and the risk assumed by the Petitioner before the sale of the leather out of which the accounts arose was made (R. 58-9; 131-3).

(e) Petitioner had advertised in a Luray, Virginia newspaper that Deford was assigning its accounts receivable and pledging its hides and leather pursuant to the factoring arrangement (Dfts. Ex. F, R. 246).

(f) These accounts receivable arose out of the sales of finished leather in warehouses leased to Petitioner

which leather, under the foregoing contract, was intended to be pledged to Petitioner as security for advances (R. 63; Dfts. Ex. A, R. 218).

(g) The leather, out of the sale of which these accounts arose, was consigned to Petitioner on consignment sheets delivered by Deford to Petitioner (R. 52-53, 63; Defts. Ex. I, R. 266); and all such leather was *finished* (no further processing to be done) by December 1, 1937, and was in a warehouse leased to Petitioner (R. 56).

(h) The Petitioner had obtained the consent of the Federal Reserve Bank, a large creditor, to this lease (R. 39-40; Dfts. Exs. C, D, and E, R. 238, 242, 244).

(i) There were signs on the outside of the warehouse showing that the Petitioner was the factor of Deford and signs on the inside of the warehouse showing that "all leather in this warehouse is pledged to Edmund Wright Ginsberg Corporation" (R. 79-85; Dfts. Ex. O, R. 276); these signs were erected by a custodian, who was on the payroll of Petitioner, and in charge of the pledged property of the Petitioner (R. 74-85).

(j) The insurance covering the finished leather, out of the sale of which these accounts receivable arose, was payable to the Petitioner (R. 143).

(k) The consignment sheets, upon which the leather out of which these accounts receivable arose was listed, together with the monthly inventory sheets of such leather, were used by the Petitioner for determining the amount of advances to be made from time to time by Petitioner to Deford (R. 141-2).

(l) The alleged preference consisted of numerous assignments of accounts receivable on various dates during the four months period, not a single bulk assignment (Pls. Ex. 4, R. 170).

(m) Petitioner and Deford, in April, 1938 engaged in discussions and communications and proposals for reopening the plant (R. 64-71; Dfts. Exs. V and W, R. 306, 309).

(n) Reference to Petitioners' factoring of Deford's accounts and inventory appeared in the financial statements issued by Deford's accountants (Pls. Exs. 2, 3; R. 168, 342).

No evidence was introduced even tending to show that Petitioner at any time had reasonable cause to believe the assignments of the accounts receivable were preferences. "Whether such 'reasonable cause to believe' existed is a question of fact and the burden of proof is on the trustee." *Pyle* v. *Texas Transport & Terminal Co.*, 238 U. S. 90, 98 (1915). The evidence being in this state, the findings of fact should stand, and they preclude a voidable preference under Section 60(b).

IV.

Findings of fact, establishing a valid pledge were supported by substantial evidence, the weight of the evidence, and were not clearly erroneous.

The Trial Court's findings of fact IV, V, VI, VII, VIII, IX, X, XI, XVI, XVII, XXI, XXII, XXIII and XXVIII (R. 330-4) established that Petitioner had an effective pledge. These findings were supported by substantial evidence, the weight of the evidence and were not clearly erroneous. The Circuit Court of Appeals, without mentioning any of the findings of fact, and ignoring Rule 52(a) gave as its principal ground for holding the pledge invalid, the inadequacy of the signs indicating that the property was pledged (R. 348). Contrary to the opinion of the Circuit

Court of Appeals, in addition to the evidence summarized above (*ante,* pp. 23 to 25), there was the following abundant evidence showing the property was pledged to the Petitioner:

Signs were placed on the five buildings leased to Petitioner. They were placed "right on the door" (R. 84). There was also a sign on the door of the main tannery office building ("It was on the front door") (R. 84), identified as building No. 4 on Defendant's Exhibit D (R. 80). The signs were on the doors of the three warehouses and the warehouse office (R. 102, 107, 99), (see Pls. Ex. 13, R. 188); outside the hide house, leased to Petitioner, annexed to the door (see Pls. Ex. 24, R. 210); The sign read "Edmund Wright Ginsberg Corporation, Factor for The Deford Company" (see Dfts. Ex. O, R. 276). Mr. Long helped put up cardboard signs about November 1, 1936 (R. 80-81). Subsequently they were replaced with brass plate signs, of which Defendant's Exhibit O is one (R. 81, 276).

The signs may also be noticed, in spite of obviously poor photography, in the pictures introduced as Plaintiff's Exhibit 13 (R. 188), on Building No. 25; Plaintiff's Exhibit 14 (R. 191), on Building No. 22; Plaintiff's Exhibit 17 (R. 197) on Building No. 55; and Mr. Long marked Plaintiff's Exhibit 22 (R. 207) where he had placed a sign on Building No. 17 (R. 107-8). On Plaintiff's Exhibit 24 (R. 211), the picture of the hide house which did not show signs (there was no evidence as to when the pictures were taken), Mr. Long marked on the hide house where one of the brass signs had been placed (R. 125).

The signs inside the warehouse read, "All leather in this warehouse is pledged to Edmund Wright Ginsberg Corporation" (R. 81), and were "white with black letters" (R. 83). These signs were located in "the most conspicu-

ous place we could put them" (R. 84). In Warehouse No. 22, the sign was placed "right ahead of you" as you were entering the door (R. 84); on Warehouse No. 17, it was placed on "a little partition" (R. 84); and on Warehouse No. 55, it was placed on a cupboard (R. 84). The witness frequently indicated just where the signs would be, and the Trial Court saw him make these indications. For instance,

> "Q. Where was the entrance to these warehouses? A. The entrance, right there (indicating).
>
> Q. No. In relation to the sign, when you came in the entrance, where would the sign be? A. Right on the door. You mean on the inside or out?
>
> Q. The inside signs? A. Oh, the most conspicuous place we could put them.
>
> Q. Well, where would they be? Try to tell us. A. Well, if you walk in this door going this way (indicating) the sign was right up there (indicating), on a little shelf. We had it there where the motor was, and right in front of the door, and in the other one, the warehouse, up here (indicating)" (R. 84).

So that the Trial Court, when it made its findings of fact that these signs were in conspicuous places, had the benefit of hearing the witness testify and seeing the indications he made, and was better able to conclude as to whether the signs were conspicuous, than was the Circuit Court of Appeals.

To overcome this overwhelming evidence of notice of the pledge, the Plaintiff offered evidence that there was a small sign saying the premises were private and belonged to Deford (Pls. Ex. 8, R. 178); large signs on the side of a building and the water tower carried the name of Deford (Pl. Exs. 9 and 10, R. 180-2), and there was a screen door in front of the door on which one of Petitioner's signs appeared (Pl. Ex. 12, R. 186). Obviously, if there are signs

on the buildings in which the pledged property is located giving the requisite notice, it is certainly not legally necessary to take down all the signs carrying pledgor's name on every other building on the premises. In the instant case, only five out of some thirty buildings were leased by Deford to Petitioner to be used in connection with the pledged leather. Petitioner was not required to usurp the functions of Deford for the business was that of Deford and not of Petitioner. See: *In re Nathan and Cohen,* 58 F. (2d) 670 (S. D. N. Y., 1932), reversed on another point 68 F. (2d) 864.

With respect to the screen on the door on which a sign of Petitioner appeared, it should be noted that this concerned an inconspicuous building which was the office occupied by Kendrick and Mr. Long, as custodian for the Petitioner (Dfts. Exs. C and D, R. 238, 242). More important, is that the sign was perfectly clear when the screen door was open (Pls. Ex. 13, R. 188) and the screen was tied back during the winter (R. 122). Moreover, how could one enter the building without opening the screen door?

It is most significant that there was a sign on the *main office building,* not even leased to Petitioner. "It was on the front of the door when you go in" (R. 80).

Erroneously reviewing the evidence *de novo* and ignoring Rule 52(a), the Circuit Court of Appeals also said:

> "Not even the attempted possession, apart from notice, comported with the traditional common law rules. One of Deford's employes was switched to defendant's payroll and made custodian of the pledged hides. But except for making some notations in a small note book, he continued his work as before. All other activity continued as formerly except as to actual sales, which had to be approved

by defendant. Even though the custodian was given a set of keys to the leased buildings, three other sets remained in Deford's hands; and although the custodian was supposed to unlock and lock the premises, it appears that he did so only when he was the first to arrive or the last to leave. There was also a small stamp, consisting of a circle around a cross, placed on each hide to indicate that the hide was pledged; but the stamp seems always to have been around the premises, and use of it appears to have differed only in that after the pledge arrangement every hide was stamped. Thus, the attempted legal shift of control was little more than a matter of lip service to the rules'' (R. 348-9).

The Trial Court's findings of fact with reference to the above are numbers XII, XIII, XIV, XV, XVI, XVII (R. 332). These findings are supported by substantial evidence, which shows that Long was employed as custodian for your Petitioner (R. 74), in deliberate preference to Kendrick, who was frequently absent from the premises (R. 77); that he was instructed as to his duties (R. 76); paid his salary by Petitioner (R. 74); had a Social Security card, which showed on the bottom of it the name of Petitioner, as his employer (R. 74; Dfts. Ex. N, R. 274); that his salary was charged back to Deford from November 1, 1936 to December 31, 1937, *but there was no charge-back whatsoever after December 31, 1937* (R. 142); Long did not know that his salary was ever charged back, for any period, by Petitioner to Deford (R. 119-20); that when hides came to the plant, Mr. Edmundson, Assistant Superintendent of the tannery, would let Long know, and Long would go to the hide house, as he was instructed (R. 87), look at the hides, and take the record of them from Mr. Edmundson (R. 89); he told Mr. Edmundson he represented Petitioner (R. 78); he told Kendrick of his visits to the hide house (R. 159); he also

went to the beam house two or three times a week (R. 78), and inquired of Mr. Osborne, the beam house foreman, if he had put the monogram (Dfts. Ex. B, R. 237), on all the hides, and he said he had (R. 77). Long saw the stamp put on some of the hides at different times (R. 77). After his employment as custodian, as a part of his duties Long kept a record in a note book (Dfts. Ex. P, R. 279) both for his own information and for the information of your Petitioner, of the number of hides that were on hand in the hide house, the number that were delivered to the beam house to be worked through the tannery, together with the Deford stamp number or lot number, and the symbol of your Petitioner (R. 87-8; Dfts. Ex. P, R. 279). When the hides were through the process of tanning and came out as finished leather, they were delivered to the warehouse, where Long checked the pieces of leather received with the hides that had been processed, to see that the bends and the rest of the leather tallied with the number of hides that had been worked in the tannery (R. 90). The symbol used was a stamp of a cross in a circle (Dfts. Ex. B, R. 237), on the back of which was a typewritten notice reading: "Imprint of pledgee to identify pledged property in process of manufacture", and was signed by Thomas Deford, Vice President of Deford, and Jacob Ginsberg, President of your Petitioner. We submit that this evidence supports the findings of the Trial Court, and that Long did more than make mere entries in a note book, as stated by the Circuit Court of Appeals and furthermore, that the symbol which had been used prior to November 1, 1936, had only been used on "hides that were financed a certain way", and, quite properly, after November 1, 1936, was adopted by the parties and put on all hides which were financed by Petitioner.

Long testified when he came to work each morning at seven o'clock, the entrance doors to the warehouse were locked and he unlocked them, and when he quit work each night at five o'clock he locked the entrance doors himself or saw that they were locked (R. 87).

This testimony together with his testimony on cross examination (R. 115-6) did not justify the Circuit Court of Appeals in drawing the following inference inconsistent with the findings of the Trial Court:

> "* * * although the custodian was supposed to unlock and lock the premises, it appears that he did so only when he was the first to arrive or the last to leave." (R. 349.)

As to the Circuit Court of Appeals' statement (R. 348-9) that all activity continued as formerly, except as to approval of sales by the Defendant, consider the facts of the Petitioner's signs on the premises; the lease of buildings to the Petitioner and the assent thereto by a large creditor-mortgagee of Deford; the contract between Deford and Petitioner; the credit reports disclosing the transaction; reference to the transaction in Deford's financial statements; the advertising of the transaction in compliance with the Virginia Traders Act; the regular periodic consignments of leather to the Petitioner; the regular periodic assignment of accounts to the Petitioner; the invoices of Deford, showing the accounts were assigned to and exclusively payable to Petitioner; no sales of leather being made without the approval of Petitioner; the above activity of the custodian, and numerous other changes related above (*ante*, pp. 23 to 25).

The Circuit Court has also said that: "All the acts here recited are conceded by the parties in a well presented case". (R. 349.) No such concession was or is made by

Petitioner because it sharply disagrees with the Court's characterizations and inferences with respect to notoriety and possession.

In summary, the findings of fact establishing an effective pledge were supported by substantial evidence, the weight of the evidence, and were not clearly erroneous. The Circuit Court of Appeals, reviewing the evidence *de novo,* failed to give due regard to the opportunity of the Trial Court to judge of the credibility of the witnesses, disagreed with the findings, and reached a conclusion which set them aside. In doing so, it violated Rule 52(a) of the Federal Rules of Civil Procedure and exceeded its power. See *Webb* v. *Frisch,* 111 F. (2d) 887 (C. C. A. 7th, 1940).

V.

The Circuit Court of Appeals, in deciding that a pledge may not be perfected by taking possession of the proceeds of the pledged property, held contrary to the applicable decisions of this Court and in conflict with decisions of other Circuit Courts of Appeal.

The contract between Deford and Petitioner (R. 218 at 228) provided (1) for a pledge of hides and leather as security for Petitioner's advances to Deford, and (2) that Deford was to sell the finished leather subject to Petitioner's approval of credits and prices, and all accounts receivable arising therefrom were immediately to become Petitioner's property.

Admittedly, Petitioner took possession of the accounts receivable in question. Deford assigned them to Petitioner, and the debtors were notified thereof, and made payments to Petitioner.

Unquestionably there was an attempted pledge of the leather prior to the four months' period. Under the au-

thorities of this Court, if such pledge were imperfect, it was perfected by Petitioner's taking possession of the proceeds (accounts) under the doctrine of relation back. *Thompson* v. *Fairbanks,* 196 U. S. 516 (1905); *Finance and Guaranty Company* v. *Oppenhimer,* 276 U. S. 10 (1928). On this point, the Circuit Court of Appeals said:

> "Finally, defendant argues that the assignments of accounts during the four months preceding bankruptcy relate back to the date of the agreement. This is clearly erroneous. In 1936, there was only an agreement to assign and, as we have held, no valid lien upon the hides and leathers. Hence, until the accounts came into existence, no security could exist; and until actually assigned, the security interest did not exist. *Okin* v. *Isaac Goldman Co.,* 2 Cir., 79 F. 2d 317; *In re Modell,* 2 Cir., 71 F. 2d 148. When the assignment was made, a preference was created. Under §60b, 11 U. S. C. A. §96b, this was voidable. Nor can the procedure followed be fairly assimilated to the taking of actual possession under an equitable pledge, for that never happened. Instead, Deford delivered possession to its vendees; and having thus created a new property in itself, by way of claim against the vendees, it assigned that to defendant. Thus fairly considered, there were two separate steps, not merely the one step of perfecting a heretofore imperfect pledge." (R. 350-1.)

The Circuit Court of Appeals obviously erred when it stated "until the accounts came into existence no security could exist". Prior to the four months' period (December 1, 1937) all leather was finished and in the warehouse (R. 56); the pledge could and did attach thereto. This leather was the fund pledged—the accounts, the proceeds thereof. The Court's reasoning that the pledge of the leather and the transfer of the accounts "were two separate steps, not

merely one step of perfecting a heretofore imperfect pledge" is unrealistic and unsound.

The Circuit Court of Appeals recognized that taking possession of the leather within the four months' period would perfect the pledge, but distinguishes the taking of possession of the proceeds. The distinction is untenable and in conflict with the cases.

In *Sawyer* v. *Turpin,* 91 U. S. 114 (1875), a valid chattel mortgage given and recorded within the four months period was exchanged for an unrecorded bill of sale in the nature of a chattel mortgage, which was invalid as to lien creditors, but valid as to general creditors of the mortgagor. The Court held the chattel mortgage was not a preference, saying:

> "It is too well settled to require discussion, that an exchange of securities within the four months is not a fraudulent preference within the meaning of the Bankrupt Law, even when the creditor and the debtor know that the latter is insolvent, if the security given up is a valid one when the exchange is made, and if it be undoubtedly of equal value with the security substituted for it."

In the instant case, the pledge, like the bill of sale in *Sawyer* v. *Turpin,* was valid between the parties. The assignment of the accounts, like the chattel mortgage, was merely a substitution of more effective legal security. Accordingly the decision of the Circuit Court of Appeals is in direct conflict with that of this Court in *Sawyer* v. *Turpin.*

In *Page* v. *Rogers,* 211 U. S. 575, 579 (1909) this Court stated:

> "It may be assumed, without decision, that the payment within four months of bankruptcy of a mortgage older than four months, and valid *inter partes,* though unrecorded, cannot be a preference."

The decision of the Circuit Court of Appeals is in direct conflict with the Eighth Circuit Court of Appeals in *Britton* v. *Union Investment Company,* 262 Fed. 111 (1919), cert. den. 252 U. S. 580, which held that the taking of possession by a pledgee of the proceeds of grain, imperfectly pledged outside of the four months' period because of the failure of possession, was not a preferential transfer, as the taking of possession of the proceeds related back to the date of the advance on the pledged property. The Court said:

> "The grain was, with the consent of appellee and the bankrupt, sold by the committee, and the resulting funds turned over to it by the committee, to be applied to its debt under the above contract. *In essence such transactions amount to a reduction to possession of the grain, and a realization thereon by it.* This entire transaction was fully consummated before the bankruptcy proceedings were initiated. Although they took place within four months of bankruptcy, yet, *for preference purposes, they relate back to the date of the contract which they were designed to and did fulfill.* Security Warehousing Co. *v.* Hand, 206 U. S. 415, 423, 27 Sup. Ct. 720, 51 L. Ed. 1117, 11 Ann. Cas. 789. Even if the contract were unenforceable, which we do not decide, as contended for by appellant, because the receipt failed to conform to the state laws governing grain warehouse receipts, yet it was not inherently vicious, was made and carried out in good faith, and had been fully performed before the bankruptcy proceedings began. Equity will not disturb such a situation. *The saving element here, which prevents application of the state statutes invoked by appellant, is that possession of the pledge became effective through possession of the money for which the same was sold* by consent of pledgor and pledgee, with the knowledge that such disposition was to be made of the money." (Italics ours.)

Similarly, in *Border National Bank* v. *Coupland,* 240 Fed. 355 (C. C. A. 5th, 1917), the Circuit Court of Appeals for the Fifth Circuit held not preferential a chattel mortgage given and recorded within the four months' period in substitution for a verbal mortgage valid as between the parties, and as against general creditors, but not against lien creditors.

The decision of the Circuit Court of Appeals is likewise in conflict with the First Circuit Court of Appeals in *Crosby* v. *Packer,* 22 F. (2d) 611 (1927). There, a guardian had borrowed money from the estate of his ward, orally agreeing that certain real estate he owned should be held as security for the indebtedness. During the four months preceding his bankruptcy he sold this real estate and deposited the proceeds thereof in his ward's bank accounts. The Court held that these payments were not preferential transfers, because an equitable interest had been granted outside the four months period to which the payment of the proceeds of the property related back.

Coppard v. *Martin,* 15 F. (2d) 743 (C. C. A. 5th, 1926), cert. den. 273 U. S. 753 (1927) likewise is contrary to the decision in the instant case. It is explained in a Note in 28 Columbia Law Review 943, at page 945 as follows:

> "An agreement to repay from the proceeds of a sale of specified goods may be equivalent to an agreement that the goods constitute a security *res,* and the debtor the creditor's agent to sell and turn over the proceeds. If this latter is done, it is the equivalent of possession in the creditor, and so may be related back."

The Circuit Court of Appeals for the Second Circuit itself held in *Irving Trust Co.* v. *Bank of America Nat. Ass'n.,* 68 F. (2d) 887 (1934) that taking possession of the

proceeds of an imperfect pledge perfects the pledge. The Court said:

> "Since delivery of the securities themselves would not have been a preferential transfer to the lienor, the delivery of their proceeds, pursuant to the agreement, could not be. Sexton *v.* Kessler & Co., 225 U. S. 90, 97, 32 S. Ct. 657, 56 L. Ed. 995; Richardson *v.* Shaw, 209 U. S. 365, 28 S. Ct. 512, 52 L. Ed. 835, 14 Ann. Cas. 981."

It is submitted that there can be no logical reason for a different result to follow from taking possession of the proceeds of leather than from the taking possession of the leather itself. The decision of the Circuit Court of Appeals on this point is clearly erroneous, and conflicts with the decisions of this Court and with decisions of Circuit Courts of Appeal discussed above.

For the reasons above set forth, it is respectfully submitted that this petition should be granted.

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